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AGENDA ITEM 3-C

**TO: MEMBERS OF THE BENEFITS AND PROGRAM ADMINISTRATION
COMMITTEE**

- I. SUBJECT:** SB 1443 (Ashburn) - As Amended June 7, 2006
Public Employees' Retirement: Maximum Retirement Allowance
- II. PROGRAM:** Legislation
- III. RECOMMENDATION:** Neutral

This legislation would cap the cumulative retirement allowance under multiple retirement formulas for individuals serving the State of California in the state patrol, peace officer/firefighter, or state safety membership categories. Although established by statute, the formulas are also subject to collective bargaining agreements.

IV. ANALYSIS:

This bill would only apply to retirements whose effective date is on or after the effective date of this measure and would limit a retirement benefit allowance based on a combination of service with the State of California in the member classifications of patrol member, state peace officer/firefighter, and/or state safety to no more than 90 percent of final compensation. SB 1443 is an urgency measure and would become effective on the date it becomes enacted.

Background

Service retirement benefits are based on several factors: age at retirement, years of service, and final compensation. The applicable benefit formula determines the benefits payable to employees. Multiplication of a "Benefit Factor" (for a particular retirement formula) based on age at retirement by the years of service under this retirement formula determines a percentage, which is then multiplied by the final compensation to determine the member's Unmodified Retirement Allowance. The

retirement benefits of safety members, however, have a statutory maximum percentage (referred to as a “cap”), that limits the percentage of final compensation that can be paid, depending on the safety employee’s classification. The benefits of state safety employees are capped at 80 percent, while the benefits of patrol members and peace officer/firefighters (PO/FF) are capped at 90 percent.

Once a safety member has worked long enough to reach the applicable cap, working additional time does not result in a higher service retirement benefit, except to the extent his or her final compensation increases. The time it takes for a safety member to reach the cap depends on the applicable benefit formula and years of service.

The Legislature adopted several Government Code sections in 1999 and 2002 which contain separate benefit formulas with separate caps for specified CalPERS membership categories. These sections provide that the benefit should be calculated applying a separate cap as specified in each Government Code section. However, all service of a member that falls under the same Government Code section and thus have the same benefit formula must be aggregated and capped at the specified percentage of final compensation.

Currently, if a State member has service under multiple safety benefit formulas in the member classifications of patrol member, state peace officer/firefighter, or state safety there could be more than one maximum benefit cap applied allowing the member’s retirement allowance to be greater than 90 percent.

Proposed Changes

This bill would only apply to retirements whose effective date is on or after the effective date of this measure and would limit the cumulative retirement benefit allowance based on a combination of service with the State of California in the member classifications of patrol member, state peace officer/firefighter, and/or state safety to no more 90 percent of final compensation. As an urgency measure, SB 1443 would become effective on the date it is enacted.

Legislative History

2003 SB 53 (Dunn)—Would have increased the retirement benefit for local safety members from 90 percent to 100 percent of final compensation for those members who retire on or after January 1, 2004, among other provisions. The bill failed passage. *CalPERS’ position: Neutral.*

SB 100 (Dunn)—Similar to SB 53 (Dunn, 2003), would have increased the retirement benefit for local safety members to 100 percent of final compensation who retire on or after January 1, 2004. The bill failed passage. *CalPERS’ position: Neutral.*

2001 Chapter 1 (SB 65, Burton)—Provided a 3 percent at age 50 retirement formula for state peace officer/firefighter (PO/FF) members who are members of State Bargaining Unit 6 and who retired or died on or after January 1, 2006, among other provisions. *CalPERS' position: None.*

Chapter 56 (SB 183, Burton)—Made the 3 percent at 50 years of age retirement formula applicable to state PO/FF members who are members of State Bargaining Unit 7 and who retire or die on or after July 1, 2004 among other provisions. *CalPERS' position: Neutral*

Chapter 796 (SB 90, Dunn)—Increased the maximum retirement allowance to 90 percent of final compensation for local safety members who retired on or after January 1, 2002. *CalPERS' position: Neutral.*

1999 Chapter 555 (SB 400, Ortiz)—Added the Sargeants-at-Arms of each house of the State Legislature, excluding the Chief Sargeant-at-Arms, within the PO/FF category. Prescribed a 3 percent at 50 formula for member of the California Highway Patrol and a 3 percent at 55 formula for state PO/FF members and certain local safety members, among other provisions. *CalPERS' position: Sponsor.*

Chapter 633 (SB 800, Dunn)—Increased retirement allowance limits for local safety members to 85 percent for those who retire on and after January 1, 2000, among other provisions. *CalPERS' position: Neutral.*

1994 Chapter 762 (AB 2801, Brown)—Increased the maximum retirement allowance from 75 percent to 80 percent of final compensation for local safety members who retired on or after January 1, 1995.

Issues

1. Arguments in Support

The author states that, “due to a change in the pension formula for rank-and-file firefighters a loophole opened earlier this year that allowed some supervisors who had formerly worked as firefighters to qualify for pensions that far exceeded their top salary. Under this loophole some retiring state firefighter managers will receive as much as 115 percent of their final salaries. This translates in real terms to mean a firefighter earning a top salary of \$95,000 could walk away with a pension of \$102,000 a year. For this very reason, the author has introduced SB 1443 which proposes to close this loophole and reinstate the original maximum cap of 90 percent. This measure is simply intended to restore equity within the firefighter pension system.”

2. Arguments by those in Opposition

There is no known opposition at this time.

3. Implementation Issues

SB 1443 is an urgency statute, so CalPERS would need to be prepared to implement the changes as soon as the bill is enacted. Information Technology (IT) resources will be needed to update the systems that staff use to estimate and calculate retirement and death benefit allowances and the systems used for service credit cost calculations. If these system changes cannot be timely implemented, staff would be required to manually process retirement and death benefit calculations and service credit cost calculations affected by this legislation.

4. Vested Rights

Public employees who render services under pension statutes secure vested pension rights. An employee's vested right is limited, however, by the express conditions contained in the pension law at the time of commencement of employment, or reasonably added to the law after employment. A change to retirement laws that diminishes earned pension rights of public employees may violate the constitutional prohibition against impairment of the obligation of contracts. However, changes may be made in earned pension rights of active employees if the pension law in place specifically authorizes the change in benefits, or if the changes are reasonable and related to the theory of a sound pension system, and if the disadvantages are offset by comparable new advantages to employees.

The amendments made by SB 1443 are stated to be declaratory of existing law. It is anticipated that if the bill becomes law, it may be challenged as constituting an impairment of vested pension rights. CalPERS cannot predict whether such a challenge might be successful or whether a court might either (i) concur that SB 1443 is declaratory of existing law or (ii) uphold SB 1443 upon finding that changes in earned pension rights of active employees are reasonable and related to the theory of a sound pension system and that the disadvantages are offset by comparable new advantages to such employees.

5. Legislative Policy Standards

The Board's Legislative Policy Standards suggest a neutral or no position on proposals to change retirement benefits which are appropriately subject to collective bargaining and are consistent with other Board policies. Additionally, based on the legislative history, the Board has historically adopted either a

neutral or no position on proposals that dealt with the retirement benefit cap which is what this bill would do.

V. STRATEGIC PLAN:

This item is not a specific product of the annual or strategic plans, but is part of the regular and ongoing workload of the Office of Governmental Affairs.

VI. RESULTS/COSTS:

Limiting a retirement or death benefit allowance based on a combination of service with the State of California in the member classifications of patrol member, state peace officer/firefighter, and/or state safety to 90 percent of final compensation would have a minimal impact on employer costs. CalPERS would incur minimal IT costs to update systems used to estimate or calculate retirement or death benefits.

Program Costs

SB 1443 would have no immediate impact on the required State contribution to CalPERS. Cost savings would be anticipated but not until the time a State member retires with a benefit capped as a result of SB 1443. These savings would appear in the form of demographic gains and would be amortized over a 30 year period in accordance with the CalPERS Board policy on amortization. As a result, savings from SB 1443 will be immaterial to the overall State contribution to CalPERS toward pension benefits.

Administrative Costs

This bill would require changes to the systems that estimate and calculate retirement allowances. The costs of these system changes are expected to be minimal.

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